

**SOAH DOCKET NO. 582-11-1468  
TCEQ DOCKET NO. 2010-1841-UCR**

<b>APPLICATION OF SJWTX, INC, DBA</b>	<b>§</b>	<b>BEFORE THE STATE OFFICE</b>
<b>CANYON LAKE WATER SERVICE</b>	<b>§</b>	
<b>COMPANY TO CHANGE WATER</b>	<b>§</b>	<b>OF</b>
<b>RATES; CCN NO. 10692; IN COMAL</b>	<b>§</b>	
<b>AND BLANCO COUNTIES</b>	<b>§</b>	<b>ADMINISTRATIVE HEARINGS</b>

**CEWR'S REPLIES TO EXCEPTIONS TO THE  
SUPPLEMENTAL PROPOSAL FOR DECISION AND PROPOSED ORDER**

TO THE HONORABLE COMMISSIONERS OF THE TEXAS COMMISSION ON ENVIRONMENTAL QUALITY:

The Coalition for Equitable Water Rates ("CEWR") respectfully submits its Replies to Canyon Lake Water Service Company's Exceptions to the Supplemental Proposal for Decision and Proposed Order, and in support of its exceptions would show the following:

**I. Introduction**

The Commission remanded this matter to SOAH to change one allocation factor used to determine the allowable amount of corporate pass-through expenses and to make the appropriate changes flowing from the change in the allocation factor. The Commission also directed the ALJs to use the ALJs' recommended rate base, except if the rate base needed to be changed because of the possible double removal of the Startzville wastewater plant.

The ALJs directed the parties to meet to resolve the factual issues and took two rounds of briefing from the parties on the issues. In the supplemental PFD, the ALJs made the change to the allocation factor and the appropriate flow through changes.<sup>1</sup> The ALJs also found that Startzville was not removed twice from rate base. Neither the Executive Director nor CEWR filed exceptions to the supplemental PFD. CLWSC, however, filed lengthy exceptions raising errors far beyond the scope of the limited remand.

CLWSC's exceptions do nothing more than reurge the arguments previously made to the ALJs. CLWSC argues that the rate base in the PFD is based on erroneous exhibits, yet CLWSC does not explain how these exhibits are erroneous. CLWSC did not object to the introduction of the exhibits and had the opportunity to cross-examine the supporting witness and to offer rebuttal testimony to fix any "errors" in the ED's exhibits. Even if CLWSC had a valid substantive position, which it does not, CLWSC waived any argument it had regarding the accuracy of the ED's exhibits by not challenging the exhibits at hearing.

---

<sup>1</sup> While CEWR may disagree with some of the details of the ALJs flow through calculations, CEWR is not pursuing further challenges of these issues because this case needs final resolution in a timely fashion.

CEWR believes that a little reminder of the history of this case and the context of these exceptions would be helpful to the Commission. CLWSC faults the ALJs for some alleged inconsistencies in the net book value of CLWSC's assets. CEWR is amazed at CLWSC's audacity in claiming the ALJs (and the Executive Director) erred when CLWSC wholly failed in its obligation to provide this data initially. CEWR finds CLWSC's focus on "math errors" absurd in light of the fact that CLWSC's rate base is "overstated" by at least \$11,097,000 in contributed assets.<sup>2</sup> CLWSC never attempted to determine or remove pre-acquisition contributed assets and as found by the ALJs, **CLWSC failed to meet its burden of proof as to rate base valuation.**<sup>3</sup> The real reason why the "rate base must be fixed" is to remove the contributed assets that lawfully should not be included in rate base, not simply to raise CLWSC's revenue requirements just enough to allow it assert a claim for rate case expenses.

## II. Rate Base Errors

CLWSC complains of numerous errors in the rate base – far more than the alleged double recovery of the Startzville plant. As the ALJs properly note in the supplemental PFD, CLWSC's arguments go far beyond the scope of the remand. The ALJs are correct in not addressing the arguments. CLWSC's failure to raise any math "errors" in the rate base in the prior exceptions (or the previous overruling of the exceptions by the Commission) preclude their "correction" now.

The ALJs reviewed the record and properly determined that the record does not support a conclusion that the Startzville plant was removed twice from the rate base. The issue of whether the Startzville plant was properly removed from rate base is question of proof. The evidence in the record shows that it was removed because the plant was not related to providing water utility service. Nothing in the evidentiary record suggests that it was not removed properly.

The rate base number in the supplemental PFD originated in the Executive Director's Exhibits ED-KA-2 and ED-KA-6. The Executive Director offered these exhibits through his expert witness Kamal Adhikari. In his testimony, Mr. Adhikari stated that he removed the Startzville wastewater plant. He did not state that he removed it twice.<sup>4</sup> CLWSC did not object to the admission of these exhibits. CLWSC cross-examined Mr. Adhikari regarding these exhibits. CLWSC did not raise an issue regarding double-removal of the Startzville plant during

---

<sup>2</sup> PFD, p. 40.

<sup>3</sup> PFD, p. 40.

<sup>4</sup> Exhibit ED-KA-1, p. 9-12.

this cross-examination. CLWSC put on rebuttal testimony. CLWSC did not raise an issue regarding the double removal of the Startzville plant during its rebuttal testimony. The question of whether the Executive Director properly removed the Startzville plant (while making the other adjustments necessitated by CLWSC's insistence on claiming inflated values for its assets) is a question that can only be resolved through expert opinion testimony. CLWSC failed to offer expert testimony even suggesting that the Executive Director's rate base was incorrect because of the double removal of the Startzville plant. This should be end of the inquiry.

CLWSC's argument fails on the substance as well. If it could be revealed by record evidence, CLWSC should be able to easily point out the error in its exceptions. CLWSC does not do this. CLWSC does not show how the Executive Director actually doubly-removed the Startzville plant. Rather than merely increasing the rate base by \$401,133 (the maximum effect the double removal could cause) and correspondingly increasing revenue requirements by the return on that amount, CLWSC merely states that the numbers do not "reconcile" that CLWSC cannot "definitively determine," and that source of the problems is "unclear."

CLWSC had the burden of proof on this issue, not the Executive Director.<sup>5</sup> Whatever problems exist in the numbers, or in the math, buried in this case, the problems are of CLWSC's own making. CLWSC had the obligation to provide the necessary documentation to support its rate base.<sup>6</sup> CLWSC filed an application that did list the original cost of the pre-acquisition assets, as required by TCEQ's application instructions. Rather, CLWSC filed an asset listing that ignored the book value of these assets in favor of artificially calculated (and inflated) "trended cost" values, and filed it in such a manner as to make it nearly impossible to analyze. Whatever CLWSC's motivation for filing its application without the book values, CLWSC's actions have muddied the record in this case from the outset. CLWSC's asset list also included that Startzville Wastewater Treatment Plant. This was another "mistake" made by CLWSC that had to be corrected through the contested case process.

Throughout this entire proceeding, CLWSC refused to provide a clean schedule of assets that could be reviewed by the parties. CLWSC never proffered testimony setting out the book value of its pre-acquisition assets. CLWSC included the value of its wastewater plant in its rate base. CLWSC objected to the Executive Director and CEWR's arguments that book value should

---

<sup>5</sup> 30 TAC 291.25(c).

<sup>6</sup> *Texas Alarm and Signal Ass'n v Public Utility Comm'n*, 603 S.W.2d 766, 772 (Tex. 1980) ("the burden of proof of the utility includes the obligation to produce relevant information").

be used for the pre-acquisition assets and objected to the book values provided by the Executive Director and CEWR. CLWSC even objected to the Executive Director's misguided attempt to "correct" its rate base schedule in its closing arguments. If the record is "cloudy" regarding rate base, the uncertainty in the rate base should work against CLWSC and not against the ratepayers. CLWSC has failed to meet its burden of proof regarding the value of its rate base.

CLWSC's exceptions simply show that CLWSC wants another chance to litigate its view of how rate base should be determined, while ignoring all other facts, such as the value of contributed assets in the rate base. CEWR is also concerned that CLWSC is attempting to again profit on confusion and slight-of-hand, in much the same way CLWSC profited by resolutely claiming that the pre-acquisition assets had no CIAC. CLWSC should not win simply because it has the resources to outlast its opposition.

Nothing in the evidentiary record suggests, much less clearly demonstrates, that the Executive Director improperly removed the Startzville plant from the rate base submitted by CLWSC. CEWR recommends that the Commission deny CLWSC's exception.

### **III. Other Supplemental PFD Errors**

CLWSC excepts to the ALJs determination that CLWSC should have to refund the entire amount that it over-collected, including the amounts that it over-collected from customers that are no longer taking service from CLWSC. CLWSC argues that its refund amount should be determined based only on current customers.

CEWR disagrees that the Commission has determined that refunds should only be made to current customers. The interim order states that the General Counsel is to modify the order to specify that overcharges "may be subject to a refund or credit to all current customers or all connections." This direction is ambiguous. The term "credit" is properly limited to "current customers" because only current customers could receive credits on their bills. "Refund" is not directly tied to "current customers," and "current" only modifies "customers" and not "all connections." The order also directs CLWSC to "calculate and account for all sums of minimum and gallonage rates overcharged *for each customer.*" If CLWSC must calculate the overcharges based on actual customer use, it follows that the Commission would want to refund these specific overcharges to the actual customers – current or former.

CLWSC has been overcharging its customers for almost three years. CLWSC should not be allowed to profit by keeping the overcollections from former customers based on an argument

that it would be difficult to determine these amounts or find former customers. CLWSC has always known that refunds might be required (and CLWSC has certainly known this since the implementation of Interim Rates). CLWSC should have maintained its records to allow any potential refunds to be made efficiently. CLWSC should not be allowed to once again benefit (as it did with regard to contributed assets) from its failure to keep proper records.

CEWR supports the refund/credit procedure contained in the supplemental PFD and proposed order.

#### **IV. New Third Court of Appeals Opinion Supports CLWSC's Recovery of Rate Case Expenses**

CLWSC asserts that a new opinion issued by the Third Court of Appeals holds that the Commission's application of the 51% rule would be unlawful because it would be "confiscatory." CLWSC's assertion is groundless. The case<sup>7</sup> cited by CLWSC (which is not yet suitable as precedent as a final decision) does not support the proposition espoused by CLWSC. It provides no basis to reverse the ALJs' recommendation. The crux of the *Oncor* case is that the PUC erred by not following its own rules and prior interpretation of the law. According to the rationale of the *Oncor* case, the Commission would err if it were to decide to abandon its 51% rule in this case simply to allow CLWSC to recover rate case expenses.

CLWSC misconstrues the ALJs' recommendations in this case. The ALJs have not held that CLWSC's rate case expenses were reasonable and necessary. Rather, the ALJs recommend finding the rate case expenses, in total, to be unreasonable and unnecessary as a matter of law because the final rate is less than 51% of the rate requested in CLWSC's application. To the extent that Findings of Fact 130 and 141 suggest otherwise, the findings should be changed.

The *Oncor* case holds that the PUC erred first in determining that it did not have jurisdiction to award rate case expenses from prior rate cases, and second that the PUC was arbitrary in limiting rate case expenses to those incurred during the test year (when the PUC had never previously imposed such a limitation). According to the court, the problem with the PUC's decision not to allow rate case expenses from previous cases to be recovered in the case under review was that the parties did not know what was expected of them in the administrative

---

<sup>7</sup> *Oncor Electric Delivery Co., LLC v. Public Utility Commission*, Slip Opinion No. 03-11-00233-CV (Tex. App. – Austin June 14, 2013).

process.<sup>8</sup> In effect, the Court reversed the agency because it changed the rules in the middle of the game.

Here, everyone knew that the 51% rule would control whether CLWSC would be entitled to recover rate case expenses. The rule has been in place since 2006, has been consistently applied by the Commission in every rate case, and was repeatedly discussed in testimony and briefing in this proceeding. The parties presented their cases and the ALJs made their rulings with the assumption that this rule was in place and controlling on the issue. It would be fundamentally unfair (and arbitrary) for the Commission to change the controlling rules of the proceeding now that the proceeding has been concluded. An agency must follow the clear, unambiguous language of its own regulation, or its action will be reversed by the courts as arbitrary and capricious.<sup>9</sup>

Disregarding the 51% rule as requested by CLWSC in its exceptions would also set bad public policy. The Commission adopted the 51% rule to address the concerns of ratepayers that by allowing utilities to always recover rate case expenses, regardless of how outrageous the rate change request, provided an incentive to utilities to overreach in their rate applications.<sup>10</sup> The purpose of the rule was to clearly set out certain instances when, as a matter of law, rate case expenses will be considered unreasonable, unnecessary, and against the public interest. The Commission concluded that if a utility could not justify even half of its proposed rate increase, then (as a matter of common sense) the utility should not be allowed to recover rate case expenses.<sup>11</sup>

If the Commission were to accept CLWSC's position and allow CLWSC to recover rate case expenses, even though CLWSC failed to satisfy the 51% rule, the Commission would be removing the strongest protection it has enacted to prevent utilities from overreaching in their rate applications. Utilities would then file even larger requests to increase rates because all litigation over the application would be borne by the ratepayers. CEWR sincerely hopes that this is not the result that the Commission desires.

If necessary to address CLWSC's argument regarding the 51% rule, CEWR recommends that Findings of Fact Nos. 130 and 141 be changed as follow:

130. CLWSC had \$856,742.42 in rate case expenses ~~that are reasonable and necessary.~~

---

<sup>8</sup> *Oncor* at 19.

<sup>9</sup> *Pub. Util. Com'n of Texas v. Gulf States Utilities Co.*, 809 S.W.2d 201, 207 (Tex. 1991)

<sup>10</sup> 31 Tex. Reg. 8107 (Sept. 22, 2006).

<sup>11</sup> CEWR would suggest that the 51% rule is far too deferential to utilities. If a utility fails to justify 100% of its requested increase it should not be allowed to recover any litigation costs associated with the rate case.

141. Because CLWSC did not meet the 51% rule, CLWSC's rate case expense are found to be unreasonable and unnecessary as a matter of law, and CLWSC is not entitled to collect any surcharge for rate case expenses.

### **CONCLUSION AND PRAYER**

After considering the foregoing, CEWR respectfully requests that the Commission adopt the ALJ's supplemental PFD, with the one modification set out herein.

Respectfully submitted,

MATHEWS & FREELAND, L.L.P.

By: 

Joe Freeland

State Bar. No. 07417500

327 Congress Ave., Ste. 300

Austin, Texas 78701

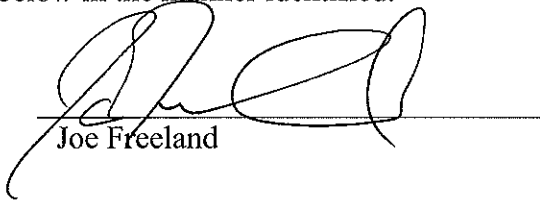
Telephone (512) 404-7800

jfreeland@mandf.com

ATTORNEYS FOR CEWR

**CERTIFICATE OF SERVICE**

I hereby certify that on this 5<sup>th</sup> day of July, 2013, a true and correct copy of the foregoing document was sent to the persons listed below in the manner identified.

  
\_\_\_\_\_  
Joe Freeland

Docket Clerk  
Texas Commission on Environmental Quality  
Office of the Chief Clerk  
PO Box 13087  
Austin, TX 78711-3087  
*Electronic Filing (7 copies sent by 1<sup>st</sup> Class Mail)*

Paul M. Terrill III  
Attorney for Canyon Lake  
The Terrill Law Firm  
810 W. 10<sup>th</sup> St.  
Austin, TX 78701  
Email to [pterrill@terrill-law.com](mailto:pterrill@terrill-law.com)

Scott Humphrey  
Office of Public Interest Counsel  
TCEQ, MC 103  
P.O. Box 13087  
Austin, Texas 78711-3087  
Email to [scott.humphrey@tceq.texas.gov](mailto:scott.humphrey@tceq.texas.gov)

Brian MacLeod  
TCEQ, MC-173  
P.O. Box 13087  
Austin, TX 78711-3087  
Email to [brian.macleod@tceq.texas.gov](mailto:brian.macleod@tceq.texas.gov)

Hon. Kerrie Jo Qaultrough & Penny A. Wilkov  
State Office of Administrative Hearings  
P.O. Box 13025  
Austin, TX 78711-2025  
*Via Web Filing*

Word version of filings sent to [Virginia.gonzales@soah.state.tx.us](mailto:Virginia.gonzales@soah.state.tx.us)